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UNCLAS SECTION 01 OF 02 COLOMBO 001717

SIPDIS

DEPT FOR EB/CBA DWINSTEAD, SA/INS
COMMERCE FOR ITA:ASTERN

SENSITIVE

E.O 12958: N/A

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SUBJECT: THE INVESTMENT CLIMATE IN SRI LANKA -
PROBLEM AREAS AND SUCCESS STORIES

1. (U) The agenda for the bilateral Trade and Investment Framework (TIFA) meeting includes an opportunity for the USG to discuss the current investment climate with the GSL. This message describes Post's experiences over the past year.

2. (U) Sri Lanka continues to offer both promise and peril for US investors. Numerous companies with products or services in traditional sectors, such as manufacturing, in Board of Investment export processing zones are successful, with little help. Other firms have needed significant Embassy advocacy to receive fair treatment (see para 5). Inefficient bureaucracies, inconsistent policies, no delegation of decision-making authority and political pressure have prevented some American companies from implementing their business plans.

3. (SBU) In the energy sector especially, US companies face bureaucratic and, it appears, politically motivated delays and non-payment. AES Power, Alstom Power Rentals and Lionvert Refineries have each experienced serious delays in project implementation and been victims of reneging on contractually agreed payment terms. Currently, the Embassy advises extreme caution for US investors in the power sector, with the primary culprit being the ineffective and, reportedly, highly corrupt, Ceylon Electricity Board. Despite repeated interventions by the Ambassador at the Minister level and to the President's Office, Post has not been able to resolve the payment disputes, though there may be some recent movement in the protracted approval process for Lionvert.

4. (SBU) Cabinet approval is required for virtually all decisions related to government spending initiatives. Several US companies have experienced project implementation delays because government Ministers simply don't present their cases to the cabinet for approval. ESP, a US company with an approved vehicle emissions testing program, is one example. Despite no cost to the GSL, and the support of numerous high-level figures in the Government (including, reportedly, the President), the Transport Minister has refused to raise the issue at Cabinet, citing worries about "political fallout." Unless Sri Lanka takes steps to develop a transparent government procurement and investment framework that can proceed with approvals far below cabinet level, it will continue to see less than optimal FDI inflows.

5. (SBU) Despite many obstacles, Post has been able to assist firms to achieve their goals. Below is a list of cases that have been supported by Post.

Success Stories

-- GTech, an online lottery service, experienced numerous difficulties, ranging from specious court cases by competitors to unfounded allegations of bidding improprieties. Embassy advocacy over the past nine months contributed to resolution, and the planned launch in December. This \$12 million investment is expected to produce revenues of \$10 million per year starting the second year.

-- Fiserv and IBM requested Embassy assistance when they felt they were not being treated fairly during a government-owned banking tender. Embassy pressure to make the choice on qualifications, rather than for political reasons, helped these firms win the \$10 million deal.

-- Commercial Lynks is the largest supplier of soybeans to Sri Lanka. This firm had numerous problems with a government tender and tariff issues, which the Embassy addressed with the GSL. They now are supplying to the market and the government without any hitches.

-- Intervention by the Embassy, including a letter from Ambassador, was credited with encouraging the resolution of a labor dispute at Energizer, which threatened to shut the factory for good. Energizer went ahead with a new \$2 million investment in the plant which supplies the local battery market.

-- Colombo Copper, a US firm successfully utilizing the Indo-Lanka Free Trade Agreement to export to India, had problems when competitors sidestepped the value-added requirements to undercut prices and swamp the market. Embassy advocacy with the Ministry of Commerce assisted in closing down these non-compliant competitors.

-- Working with the Department of Commerce's Advocacy Center, the Embassy protested against the choice of a non-competitive foreign firm for an ADB-funded port software project. Post's efforts, along with others, led to this decision being overturned, and allowed the favored US firms to compete fairly.

16. (U) USG officials could cite the first three cases during TIFA discussions for examples of successful US business endeavors, but should also note with concern the fact that US companies continue to suffer frustrating setbacks, particularly in important infrastructure sectors like energy.

Lunstead